



DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

[Docket No. FR-5723-N-01]

Federal Housing Administration (FHA): Single Family Quality Assurance - Solicitation of Information on Quality Lending Practices

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Notice.

SUMMARY: Through this notice, FHA solicits comment from its approved lenders, the lending industry generally, consumers, consumer protection agencies, and interested members of the public on ways to improve the efficiency and effectiveness of FHA's quality assurance process (QAP). The objective of FHA's QAP is to promote quality lending practices by FHA's approved lenders; practices that protect the consumer and mitigate risk for the lender and FHA. The feedback that FHA receives through this solicitation will help inform FHA of next steps that FHA may want to take to strengthen its current QAP.

DATES: Comment Due Date: **[Insert date 60 days from the date of publication in the Federal Register]**.

ADDRESSES: Interested persons are invited to submit comments regarding this document to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC 20410-0500.

Communications must refer to the above docket number and title. There are two methods for submitting public comments. All submissions must refer to the above docket number and title.

1. Submission of Comments by Mail. Comments may be submitted by mail to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC 20410-0500.

2. Electronic Submission of Comments. Interested persons may submit comments electronically through the Federal eRulemaking Portal at www.regulations.gov. HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows the commenter maximum time to prepare and submit a comment, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments submitted electronically through the www.regulations.gov website can be viewed by other commenters and interested members of the public. Commenters should follow the instructions provided on that site to submit comments electronically.

Note: To receive consideration as public comments, comments must be submitted through one of the two methods specified above. Again, all submissions must refer to the docket number and title of the document.

No Facsimile Comments. Facsimile (FAX) comments are not acceptable.

Public Inspection of Public Comments. All properly submitted comments and communications submitted to HUD will be available for public inspection and copying between 8 a.m. and 5 p.m. weekdays at the above address. Due to security measures at the HUD Headquarters building, an appointment to review the public comments must be scheduled in advance by calling the Regulations Division at 202-708-3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number via TTY by calling the Federal Relay Service at 800-877-8339. Copies of all comments submitted are available for inspection and downloading at www.regulations.gov.

FOR FURTHER INFORMATION CONTACT: Kathleen A. Zadareky, Associate Deputy Assistant Secretary for Single Family Housing, Office of Housing, Department of Housing and Urban Development, 451 7th Street, SW, Washington, DC 20410-8000; telephone number 202-

708-3175 (this is not a toll-free number). Persons with hearing or speech challenges may access this number through TTY by calling the toll-free Federal Relay Service at 800-877-8339.

SUPPLEMENTARY INFORMATION

I. Background

FHA has long required its approved lenders to maintain and implement a quality control plan (QCP).¹ A copy of the plan must be submitted by the lender when applying for FHA lender approval. FHA considers a QCP to be an important part of a lender's origination and servicing operations. The purpose of the QCP is to help ensure that the lender maintains compliance with FHA requirements and the lender's own policies and procedures. The QCP must be sufficient in scope to enable the lender to evaluate the accuracy, validity and completeness of its loan origination and servicing operations. Specifically, the QCP should be designed to meet the following basic goals: assure compliance with FHA's and the lender's own origination or servicing requirements throughout its operations; protect the lender and FHA from unacceptable risk; guard against errors, omissions and fraud; and assure swift and appropriate corrective action.

In addition to the lender QCP, FHA conducts an independent review of loan endorsements through one or more processes: post-endorsement technical reviews, Quality Assurance Division reviews and targeted lender reviews. Each of these approaches has a targeted sampling methodology. FHA also relies on certain metrics as part of its QAP. For example, for each lender, FHA computes a Compare Ratio, which measures the early default and claim rate on that lender's FHA mortgages, relative to the early default and claim rate on all

¹ See Chapter 7 of FHA's Mortgagee Approval Handbook (4060.1) at http://portal.hud.gov/hudportal/HUD?src=/program_offices/administration/hudclips/handbooks/hsgb/4060.1.

FHA mortgages in that given geographic area.

Over the last few years, FHA has taken several steps to strengthen FHA's oversight functions, and conducting an examination of FHA's single family QAP is another step in that direction. FHA is evaluating single family quality assurance alternatives that would better align with FHA's mission. Specifically, FHA seeks to ensure that it maintains and improves a quality assurance framework that does not hinder or dissuade lending to FHA-targeted populations, enhances the efficiency and effectiveness of the QAP, ensures compensation to FHA for defects resulting from the lender manufacturing process, and applies fairly to all lenders. FHA also seeks a framework that ensures that loans are reviewed within a reasonable time period, post-endorsement, to allow FHA to use loan quality findings to improve credit policy and to allow lenders to improve their FHA origination practices. Any changes initiated as a result of this solicitation will be prospective only, and will not apply to any pending claims, reviews, or enforcement actions.

II. Solicitation of Comment

As part of FHA's own evaluation of the QAP, FHA welcomes input from warehouse lenders, retail lenders, mortgage bankers, wholesale lenders, mortgage brokers, federal, state, and local consumer protection and enforcement agencies, consumer groups and other interested parties in the mortgage lending industry and the broader public. FHA specifically seeks input that addresses one or more of the following areas, which are the current focus of FHA regarding the QAP:

1. Loan defect and appropriate consequence (e.g. indemnification, other administrative remedies). What types of loan manufacturing or compliance defects found in the QAP should be subject to indemnification or other administrative remedies or a combination of responses?

2. Annual review and comparison of rate of early defaults and claims. FHA is currently required by statute to review, at least annually, the rate of early defaults and claims for FHA-insured single family mortgages originated and underwritten by each mortgagee and, for each mortgagee, to compare these rates to those of other mortgagees originating or underwriting mortgages in the same geographic area. FHA is examining how, within the current parameters, the review and comparison may achieve an improved assessment of a mortgagee's performance. For example, whether FHA should establish a specific standard of defaults and claims which mortgagees should not exceed within a given construct. This standard would be based on FHA's review of all mortgagees' performance in the area, thus undertaking the statutorily required comparative review, but would also be based on certain specified criteria that reflect generally accepted practices of prudent and responsible lending.

3. Standard of overall manufacturing quality. FHA is considering whether to establish a threshold manufacturing (or loan deficiency) risk tolerance. Such a standard might set a maximum threshold for the percent of loans with defects, or unacceptable patterns of recurring defects that, when surpassed, would automatically subject that lender to additional oversight, or trigger enforcement action.

4. Statistical sampling. FHA is also considering whether to establish a process to review a statistically significant random sample of loans for each mortgagee within a prescribed time frame after loan endorsement. Lenders would receive feedback on findings within an established timeframe. FHA would use the statistical sample, to estimate the defect rate on each lender's overall FHA portfolio and then extrapolate the origination defect rate to all lender originations during the sampled time period, and thus have the lender compensate FHA for the estimated total risk to FHA resulting from the lender's origination processes. The purpose of this process would

be to increase the efficiency of FHA's post-endorsement review process. HUD invites comment on the use of and optimal methodology for a statistically significant random sample, including the nature of the loans that should be included or excluded from the sample.

While FHA specifically seeks comment on the four areas identified above, FHA welcomes comment on all issues related to its QAP and how this process may be improved. Based on information received in response to this solicitation, FHA will decide what, if any, action may be appropriate with regard to FHA's Single Family Quality Assurance practices.

Dated: July 3, 2013

Carol J. Galante
Assistant Secretary for Housing–
Federal Housing Commissioner

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